SUPREME COURT, U. S.

FILED

MAY 29 1975

MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

No. 74-1495

FLORENCE G. SHEFNER,

Appellant,

vs.

CASPAR WEINBERGER, Secretary,

of

HEALTH, EDUCATION AND WELFARE,

Appellee,

PETITION FOR WRIT OF CERTIORARI BY APPELLANT FOR FOR REVIEW OF THE DECISION OF THE EIGHTH CIRCUIT COURT OF APPEALS

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No.

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PETITION FOR WRIT OF CERTIORARI BY APPELLANT FOR REVIEW OF THE DECISION OF THE EIGHTH CIRCUIT COURT OF APPEAL

Opinions

Decisions of the administrative judge of the defendant and its appeal counsel. The decision of the district court of the fourth district of Minnesota affirmed by the eighth circuit court of appeals without an opinion, District court decision was recorded.

Jurisdiction

Eighth circuit court decision dated March 13, 1975, filed on March 20, 1975, affirmed the district court decision dated August 12, 1974. 28 USCA Section 210 (c) rules 11 (1), 22 (1) 1967 revised rules of the Supreme Court.

Questions

Do wages not subject to F.I.C.A. taxes constitute self employment income?

Can the plaintiff's wages, which have to be included in the spouse's self employment income, be her self employment income also?

Do wages which are not subject to F.I.C.A. taxes have the same definition as wages which are the basis of benefits? Does a person have to be retired to receive benefits?

Citations

42 U.S. Code annotated
Section 403 (a) 403 (b) 403 (c) (1) 403 (f) (5) (C) 403 (k)
Section 410 (a) 410 (a) (3) (A)
Section 411 (a) 411 (C)
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Section 1402 (a) 402 (C)

Statement of the case

Plaintiff is employed by her spouse who is a self employed attorney and certified public accountant, as a secretary. The plaintiff was awarded benefits based on covered employment. The wages paid to the plaintiff by her spouse, are not subject to F.I.C.A. taxes and do not qualify as a base for determining social security benefits. The plaintiff has been denied benefits because of the wages paid to her by her spouse.

The decision of the administrative judge and of the appeals counsel of the defendant are subject to review by the district courts, by civil action commenced within 60 days

after appeals counsel decision pursuant to Section 405 (g) of Title 42 United States Code annotated.

The district court of the fourth district of Minnesota held that the plaintiff's wages constituted self employment income.

The Internal Revenue Service and the courts have taken the position that wages paid to the plaintiff are not subject to F.I.C.A. taxes and have to be included in the spouses self employment income.
The district court decision has created a new category of self employment income, which is not subject to F.I.C.A. taxes.

The administrative judges decision was based on the fact that the plaintiff's wages were not includable in her self employment income.
The plaintiff did not have self employment income, according to the facts:

Argument

Court should review the decision of the district court which holds that the plaintiff's wages constitutes self employment income.

In the case of Deputy et v. Dupont, U.S. Supreme Court 308 U.S. 488 (1940), Justice Frankfurter stated in his concurrent opinion that carrying on any trade or business within the contemplation Section 23 (a) of the Internal Revenue Code, 1921 involves one holding himself out as engaged in selling goods or services.
In the case of Whipple v. Commissioner 373 U.S. 193 (1963), the Supreme Court stated "Full time service to one corporation does not alone amount to a trade or business."

Wages do not constitute self employment income pursuant to Section 411 42 U.S. Code annotated and Section 1402 of the Internal Revenue Code of 1954, and prior codes dating back to the Internal Revenue Code of 1921. Section 411 of 42 U.S. Code annotated and Section 1402 of the Internal Revenue Code of 1954, both relate to Section 162 of the Internal Revenue Code of 1954 for the definition of self employment income. Section 162 of the Internal Revenue Code of 1954 and prior sections dating back to Section 23 (a) of the Internal Revenue Code of 1921, have held to be self employed, you have to be engaged in a trade or business.

The Supreme Court cases are legion in holding that full time employees for a corporation, partnership, or individual does not constitute a trade or business.

In the case of U.S. v. Kline (1941) 313 U.S. 127 85 LED 61 FCD 893, the Supreme Court held that in determining whether persons were conducting a trade or business, it would have to fall in the general concept of carrying on a trade or business.

The district court's decision creates further conflicts:

Section 410 (a) (3) 42 U.S. annotated excludes spouse employment as wages subject to F.I.C.A. taxes, but Section 1402 of the Internal Revenue Code of 1954, says that all self employment income is subject to F.I.C.A. taxes. Section 411 42 U.S. Code annotated and Section 1402 of the Internal Revenue Code holds that wages do not constitute self employment income.

The case of Samuel J. Cox and Martha Cox, 62TC No. 50, holds that a deduction is allowed only for wages subject to F.I.C.A. taxes in determining self employment income.

The Supreme Court stated in the case of Nierotka v. Health, Education and Welfare 327 U.S. 358 1964, that "the definition given wages under the taxing provisions should be consistent with the definition used under the qualification for benefit provisions."

It is an impossibility for the plaintiff to have self employment income for wages. The cases and the law provide that wages not subject to F.I.C.A. taxes have to be included in self employment income, by the individual who paid the wages.

For the Supreme Court to confirm the decision of the district court, it would have to find that the plaintiff paid herself wages from zero self employment, and that the wages so paid by herself would not be required to be added to nonexistent self employment income, in order to be applied as a deduction to her benefits.

Plaintiff's self-employment income would be exempt from F.I.C.A. taxes even though there is no exemption for self-employment which constitutes wages not subject to F.I.C.A. taxes.

An examination of the congressional records that are available to the plaintiff does not indicate that congress considered the question that a person has to be retired before they can be entitled to benefits. The contention of the appellee that a person has to be retired to receive benefits contradicts Section 403 42 U.S. Code Annotated.

Section 403 sets forth the conditions when deductions shall be applied to benefits which are as follows:

1) Excess wages from covered employment.

2) Engaging in noncovered activity outside the United States.

3) Substantial service rendered in connection with self employment income.

4) After the age of seventy-two, there are no deductions.

5) It is possible for a person to draw excess wages in one month which exceeds his entire benefits for the year and lose benefits for one month only.

If Congress intended that non-covered employment earned in the United States should constitute an offset to remuneration from covered employment then they would have provided for such deductions as they did in noncovered employment outside the United States. If the Court is of the opinion that the District Court decision is correct it should still allow the petition for a writ of certiorari to determine the question of what will be the basis for the plaintiff's benefits at the age of 72. The self-employment income earned in the employment of her spouse or covered employment which is the basis of the benefits being allowed.

All self-employment is subject to FICA taxes and are a basis for determination of benefits without any exception.

Dated the —— day of ——— 1975.

Respectfully submitted,

JOSEPH SHEFNER
Attorney at Law

ADDENDUM

Department of
HEALTH, EDUCATION, AND WELFARE
Social Security Administration
Bureau of Hearings and Appeals
HEARING DECISION

In the case of
Florence G. Shefner
(Claimant)

(Wage Earner) (Leave blank if same as above)
Calim for
Retirement Insurance Benefits
Wife's Insurance Benefits
(Deductions)
477-34-1256
(Social Security Number)
This case is before administrative law judge Stanley W. Ozark on a Request for Hearing filed by the claimant.

ISSUES

The general issues before the administrative law judge are whether section 203 of the Social Security Act required deductions on account of work to be made from claimant's retirement and wife's insurance benefits for the taxable years 1968 through 1971, and if so, whether recovery shall be made of incorrect benefit payments made to claimant for May 1969 and September 1970 totalling $178.30. The specific issues are whether claimant had ex-

cess earnings for all of the months of the taxable years 1968 through 1971 at least equal to the total of her retirement and wife's insurance benefits, and if so, whether claimant was without fault in accepting incorrect benefit payments for May 1969 and September 1970, and if so, whether recovery would defeat the purpose of Title II of the Social Security Act or be against equity and good conscience.

LAW AND REGULATIONS

Section 203(b) of the Social Security Act requires deductions to be made from retirement and wife's insurance benefits payable under section 202 for any month for which the beneficiary is charged with excess earnings under section 203(f).

Section 203(f) provides in effect that excess earnings for the taxable years 1968 through 1971 are earnings in excess of $1,680 except that one-half of the first $1,200 of such excess is excluded. Section 203(f)(5) provides that earnings for a taxable year are the sum of wages for services rendered in such year plus self-employment net earnings and minus self-employment net loss for such year. Section 203(f)(5)(C) provides in effect that the computation of wages for purposes of deductions from benefits shall include remuneration for services which do not constitute "employment" as defined in section 210 if such services are performed within the United States as an employee and such remuneration is not includable in computing self-employment net earnings or loss.

Section 204(a) provides for adjustment or recovery of incorrect payments of benefits. Section 204(b) provides that

adjustment or recovery of incorrect benefit payments shall not be made in the case of any person who is without fault if such adjustment or recovery would defeat the purpose of Title II or be against equity and good conscience.

Section 210(a)(3)(A) excludes from the definition of "employment" service performed by an individual in the employ of his spouse.

Section 404.429(c)(6) of Social Security Regulation No. 4 (20 CFR) provides that the computation of wages for purposes of deductions from benefits includes remuneration for services excepted from employment performed within the United States by an individual as an employee that are for that reason not considered wages under Subpart K, if the remuneration for said services is not includable in computing his net earnings from self-employment or net loss from self-employment.

Section 404.508 of Social Security Regulation No. 4 (20 CFR) provides that "defeat the purpose of Title II" means to deprive a person of income required for ordinary and necessary living expenses; and section 404.509 provides that "against equity and good conscience" means adjustment or recovery of an incorrect payment will be considered inequitable if an individual relinquished a valuable right or changed his position for the worse in reliance on such payment.

Section 404.510(n) of Social Security Regulation No. 4 (20 CFR) provides that an individual will be considered "without fault" if his acceptance of a deduction overpayment was due to failure to understand the deduction provisions of the Act and he made a bona fide attempt to restrict his annual earnings or otherwise comply with the deduction provisions of the Act.

Section 404.512(b) of Social Security Regulation No. 4 (20 CFR) provides that in the situation described in section 404.510(n) adjustment or recovery shall be waived only where the evidence establishes that adjustment or recovery would work a financial hardship or would otherwise be inequitable.

EVIDENCE CONSIDERED

The administrative law judge has carefully considered all the testimony at the hearing, the arguments made, the brief submitted, and the exhibits described in the List of Exhibits attached to this decision.

EVALUATION OF THE EVIDENCE

In a revised determination dated July 21, 1972, claimant was awarded retirement and wife's insurance benefits which it was held could not be paid to her because she had excess earnings for the taxable years 1968 through 1971. Because of said excess earnings refund was demanded of benefit payments to claimant of $81.40 in May 1969 and $96.90 in September 1970 which totalled $178.30.

The evidence shows that claimant has worked since 1956 as a secretary for her husband who is a self-employed attorney and certified public accountant, and that she was paid on a monthly basis. Her salary for the taxable years 1968 through 1971 was as follows: 1968 - $5,000; 1969 - $6,000; 1970 - $6,200; and 1971 - $6,000 (Exhibit 17, 18). Claimant testified that all her services for her husband were performed within the United States as his employee.

Claimant and her husband testified that they were on vaca-

tion during May 1969 and September 1970. Claimant's husband notified the Social Security Administration that he was entitled to his retirement insurance benefits for May 1969 and September 1970 as he was on vacation during those months. When claimant's husband received his retirement insurance benefit checks for those months, claimant also received her benefit checks for those months.

The record thus shows that claimant had earnings for all of the months of the taxable years 1968 through 1971 in excess of her retirement and wife's insurance benefits; and that such earnings were remuneration for services performed within the United States as an employee and were not net earnings from self-employment. Section 203(f)(5)(C) of the Social Security Act expressly provides, as does also section 404.429(c)(6) of Social Security Regulation No. 4, that such earnings constitute excess earnings for purposes of deductions from benefits. Accordingly, the deductions from claimant's retirement and wife's insurance benefits for all of the months of the taxable years 1968 through 1971 were required to be imposed by the applicable law and regulations; and claimant received incorrect benefit payments for the months of May 1969 and September 1970 totalling $178.30.

Claimant's counsel contends that because claimant's services performed in the employ of her spouse are excluded from the definition of "employment" by section 210(a)(3)(A) of the Act her remuneration for such services should not constitute excess earnings for purposes of deductions from benefits. He relies on *Social Security Board v. Nierotko*, 327 U.S. 358 (1946) which he cites for the proposition that the same definition must be given to "wages" for

determining qualification for benefits as for imposition of social security tax. In that case the Board determined that an award of back pay did not qualify as "wages" for purposes of old-age benefits. The Supreme Court held that the Board had exceeded the permissible limits of administrative interpretation, stating that, "Congress used a well-understood word—'wages'—to indicate the receipts which were to govern taxes and benefits under the Social Security Act." 327 U.S. at p. 369.

Unlike *Nierotko,* the issue in the instant case is not the validity of an administrative interpretation of "wages." As noted above, the Congressional definition of excess earnings for purposes of benefit deductions expressly includes, under section 203(f)(5)(C), remuneration for services which do not constitute "employment" as defined in section 210 if such services are performed within the United States as an employee and such remuneration is not includable in computing self-employment net earnings or loss. In *Gardner v. Travis,* 387 F.2d 508 (10 Cir., 1967), the Court (at p. 513) held:

> . . . Section 203(f)(5)(C) expressly makes the dictates of Section 210 inapplicable to the determination of benefit deductions. That section provides that in computing an individual's wages for the purpose of making benefit deductions, 'services which do not constitute employment as defined in section [210] of this title, performed *within the United States* by the individual as an employee * * *, shall be deemed to be employment as so defined if the remuneration for such services is not includable in computing his net earnings or loss from self-employment.' (Emphasis added) In our words, even if a service does not

> fall within the section 210(a) definition of 'employment,' section 203(f)(5)(C) requires that the wages received from the performance of that service be considered in determining whether benefit deductions are warranted. * * *

Likewise, *Ludeking v. Finch,* 421 F.2d 499 (8 Cir., 1970), held that distributed Subchapter S corporate dividends constituted excess earnings for purposes of deductions from benefits, despite the claimant's reliance on *Nierotko.* Claimant's acceptance of the deduction overpayment for the months of May 1969 and September 1970 in the total amount of $178.30 appears to be due to her failure to understand the deduction provisions of the Act, which would also explain why she has not attempted to restrict her annual earnings. Claimant has otherwise complied with the deduction provisions and thus may, under section 404.-510(n) of Social Security Regulation No. 4 (20 CFR), be considered without fault. However, there is no evidence that recovery of the overpayment would work a financial hardship on claimant or would otherwise be inequitable. Accordingly, recovery of the overpayments may not be waived.

FINDINGS

The administrative law judge makes the following findings in this case:

1. Claimant was awarded retirement and wife's insurance benefits for the taxable years 1968 through 1971.

2. Claimant had earnings for all of the months

of the taxable years 1968 through 1971 which were in excess of her retirement and wife's insurance benefits and were remuneration for services performed within the United States as an employee and were not net earnings from self-employment.

3. Deductions equal to claimant's retirement and wife's insurance benefits for all of the months of the taxable years 1968 through 1971 were required to be made from such benefits by the applicable law and regulations.

4. Claimant received incorrect benefit payments in the total amount of $178.30 for the months of May 1969 and September 1970.

5. Claimant was without fault in accepting the overpayment of $178.30.

6. Recovery of the overpayment would not defeat the purpose of Title II of the Act or be against equity or good conscience.

7. Recovery of the overpayment may not be waived.

DECISIONAL PARAGRAPH

It is the decision of the administrative law judge that because of excess earnings the retirement and wife's insurance benefits otherwise payable to claimant were subject to deductions equal to such benefits for all the months of the taxable years of 1968 through 1971; and that claimant received benefit overpayments in the total amount of $178.30. It is the further decision of the administrative

law judge that recovery of the overpayment may not be waived.

Date: Aug 29 1973.

/s/ STANLEY W. OZARK
Administrative Law Judge
Suite 830, Plymouth Building
12 South Sixth Street
Minneapolis, Minnesota 55402

Department of Health, Education, and Welfare
Social Security Administration

P.O. Box 2518, Washington, D.C. 20013

Bureau of
Hearings and Appeals

Refer to:

IHA-2
477-34-1256

ACTION OF APPEALS COUNCIL ON
REQUEST FOR REVIEW

Mrs. Florence G. Shefner
4800 Highway #7, Apt. 307
Minneapolis, Minnesota 55416

Dear Mrs. Shefner:

Your request for review of the administrative law judge's decision has been carefully considered by the Appeals Council. The Council's consideration of your request has included all the evidence in your case, the law and regulations applicable to your claim, the evaluation of the facts

and the reasoning in this decision, and your reasons for believing your claim should be allowed.

The Appeals Council has concluded that this decision is correct. Further action by the Council would not, therefore, result in any change which would be of advantage to you. Accordingly, the administrative law judge's decision stands as the final decision of the Secretary in your case. If you desire a review of the decision by a court, you may commence a civil action in the district court of the United States in the judicial district in which you reside *within sixty (60) days* from this date. See section 205(g) of the Social Security Act, as amended (section 405(g), Title 42, United States Code). If such action is commenced, the Secretary of Health, Education, and Welfare is the proper defendant.

In determining excess earnings for the purpose of imposing deductions, section 203(f)(5)(e) specifically provides that "in making such computation services which do not constitute employment as defined in section 210, performed within the United States . . . shall be deemed to be employment as so defined. . . ."

Sincerely yours,

Norman S. Karns
Member, Appeals Council

cc:
Joseph Shefner, Esquire

Memorandum Decision

Florence Shefner is in this Court pursuant to 42 U.S.C. § 405(g) seeking review of a hearing decision of Administrative Law Judge Stanley Ozark. A hearing was held before that judge to determine whether certain benefits paid to the plaintiff should be recovered by HEW and whether the plaintiff's income in recent years should be considered to be excess income so as to prevent her from receiving retirement insurance benefits. The administrative law judge held that the wages paid to plaintiff by her husband constituted excess earnings and that certain benefits paid to her would have to be returned. The Appeal Council declined to review the decision. Plaintiff now moves for summary judgment reversing the decision of the administrative law judge. The defendant has moved for summary judgment affirming Judge Ozark's determination. This Court affirms Judge Ozark's decision, grants defendant's motion for summary judgment, and denies plaintiff's motion for summary judgment.

Judge Ozark's hearing decision accurately sets forth the facts and the law applicable to this case. Certain arguments raised by the plaintiff upon this motion, however, require a response by this Court.

The plaintiff's argument has two elements. First, Mrs. Shefner argues that because employment by a spouse is not covered under the Social Security Act and wages paid thereby are not subject to FICA tax, wages paid under such employment should not be set off against her retirement benefits to defeat her rights to receive retirement benefits earned under former covered employment. As a supplement to the first argument, plaintiff argues that the statute (42 U.S.C. § 403(f)(5)(c)) regarding reductions of

benefits exempts services includable in computing net earnings or net loss from self-employment. Since the plaintiff's wages have to be included in determining her *spouse's* self-employment income, plaintiff's wages should be exempt.

With respect to the first argument, 42 U.S.C. § 410 (a)(3)(A) excludes from the definition of "employment" service performed by an individual in the employ of his spouse. Thus, wages earned in the employment of one spouse by another are exempt from FICA taxes and may not be used as a basis for determining social security benefits. Those wages, however, are specifically included within the section addressing reduction of insurance benefits. 42 U.S.C. § 403(f)(5)(C) provides that for the purposes of the subsection dealing with reductions of benefits, an individual's wages shall be deemed to be employment even if the wages are paid for services which do not constitute employment under § 410. Wages paid to a spouse, therefore, must be computed to reduce or eliminate the spouse's benefits, even if those wages are not subject to FICA taxes.

Section 403(f)(5)(C) further provides that the wages set forth above shall be considered in computing benefit reductions "if the remuneration for such services is not includable in computing his net earnings or net loss from self-employment." Plaintiff argues that the self-employment may refer both to the plaintiff and her spouse. Plaintiff admits that she has no self-employment income, but argues that § 403(f)(5)(C) does not designate whose self employment income is involved, and that when wages paid cannot be deducted from self-employment income because they are exempt from FICA taxes, then said wages are includable in self-employment income.

The short response to the plaintiff's second contention is that § 403(f)(5)(C) refers to an inclusion in his net earnings or net loss from self-employment, *i.e.*, the section refers specifically to the individual whose wages are at issue. This Court is of the opinion that the statute does designate whose self-employment income is involved and that the designation limits the reference to that income solely to the plaintiff.

The plaintiff argues that part of the payment made to her was wife's benefits and that those benefits may not be recovered by the defendant. Section 403(b) provides that "(deductions . . . shall be made from *any* payment or payments under this subchapter to which an individual is entitled. . . ." The determination of Judge Ozark shall therefore be affirmed and his determinations regarding the non-waiver of recovery of overpayment are adopted by this Court.

Plaintiff's motion for summary judgment is denied. Defendant's motion for summary judgment is granted.

IT IS SO ORDERED.

Judgment will be entered for defendant.

August 12, 1974.

/s/ EARL R. LARSON
United States District Judge

APPENDIX

United States Court of Appeals
For the Eighth Circuit

No. 74-1789

Florence G. Shefner,

Appellant,

vs.

Casper Weinberger, Secretary of Health, Education and Welfare,

Appellee.

Appeal from the United States District Court
for the District of Minnesota
Submitted: March 13, 1975
Filed: March 20, 1975

Before CLARK, Associate Justice,* LAY and BRIGHT, Circuit Judges.

PER CURIAM.

The appellant challenges the decision of the district court denying her social security insurance and retirement benefits under 42 U.S.C. § 402(a) and (b).

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*Associate Justice Tom C. Clark, United States Supreme Court, Retired, sitting by designation.

The judgment of the district court is affirmed on the basis of the well reasoned opinion of the district court.

§ 403. Reducation of insurance benefits—Maximum benefits

(a) Whenever the total of monthly benefits to which individuals are entitled under sections 402 and 423 of this title for a month on the basis of the wages and self-employment income of an insured individual is greater than the amount appearing in column V of the table in or deemed to be in section 415(a) of this title on the line on which appears in column IV such insured individual's primary insurance amount, such total of benefits shall be reduced to such amount; except that—

* * * * *

Deductions on account of work

(b) Deductions, in such amounts and at such time or times as the Secretary shall determine, shall be made from any payment or payments under this subchapter to which an individual is entitled, and from any payment or payments to which any other persons are entitled on the basis of such individual's wages and self-employment income, until the total of such deductions equals—

(1) such individual's benefit or benefits under section 402 of this title for any month, and

* * * * *

Deductions on account of noncovered work outside United States or failure to have child in care

(c) Deductions, in such amounts and at such time or

times as the Secretary shall determine, shall be made from any payment or payments under this subchapter to which an individual is entitled, until the total of such deductions equals such individual's benefit or benefits under section 402 of this title for any month—

(1) in which such individual is under the age of seventy-two and on seven or more different calendar days of which he engaged in noncovered remunerative activity outside the United States; or

* * * * *

(C) For purposes of this subsection, an individual's wages shall be computed without regard to the limitations as to amounts of remuneration specified in subsections (a), (g)(2), (g)(3), (h)(2), and (j) of section 409 of this title; and in making such computation services which do not constitute employment as defined in section 410 of this title, performed within the United States by the individual as an employee or performed outside the United States in the active military or naval service of the United States, shall be deemed to be employment as so defined if the remuneration for such services is not includible in computing his net earnings or net loss from self-employment.

* * * * *

Noncovered remunerative activity outside United States

(k) An individual shall be considered to be engaged in noncovered remunerative activity outside the United States if he performs services outside the United States as an employee and such services do not constitute employment as defined in section 410 of this title, and are not per-

formed in the active military or naval service of the United States, or if he carries on a trade or business outside the United States (other than the performance of service as an employee) the net income or loss of which (1) is not includible in computing his net earnings from self-employment for a taxable year and (2) would not be excluded from net earnings from self employment, if carried on in the United States, by any of the numbered paragraphs of section 411(a) of this title. When used in the preceding sentence with respect to a trade or business (other than the performance of service as an employee) the term "United States" does not include the Commonwealth of Puerto Rico, the Virgin Islands, Guam, or American Samoa in the case of an alien who is not a resident of the United States (including the Commonwealth of Puerto Rico, the Virgin Islands, Guam, and American Samoa); and the term "trade or business" shall have the same meaning as when used in section 162 of Title 26, Internal Revenue Code of 1954.

* * * * *

§ 410. Definitions relating to employment

For the purposes of this subchapter—

Employment

(a) The term "employment" means any service performed after 1936 and prior to 1951 which was employment for the purposes of this subchapter under the law applicable to the period in which such service was performed, and any service, of whatever nature, performed after 1950 either (A) by an employee for the person employing him, irrespective of the citizenship or residence of either, (i)

within the United States, or (ii) on or in connection with an American vessel or American aircraft under a contract of service which is entered into within the United States or during the performance of which and while the employee is employed on the vessel or aircraft it touches at a port in the United States, if the employee is employed on and in connection with such vessel or aircraft when outside the United States, or (B) outside the United States by a citizen of the United States as an employee (i) of an American employer (as defined in subsection (e) of this section, or (ii) of a foreign subsidiary (as defined in section 3121 (*l*) of Title 26, Internal Revenue Code of 1954) of a domestic corporation (as determined in accordance with section 7701 of Title 26, Internal Revenue Code of 1954) during any period for which there is in effect an agreement, entered into pursuant to section 3121(*l*) of Title 26, Internal Revenue Code of 1954, with respect to such subsidiary; except that, in the case of service performed after 1950, such term shall not include—

* * * * *

(3)(A) Service performed by an individual in the employ of his spouse, and service performed by a child under the age of twenty-one in the employ of his father or mother;

* * * * *

§411. Definitions relating to self-employment

For the purposes of this subchapter—

Net earnings from self-employment

(a) The term "net earnings from self-employment" means the gross income, as computed under chapter 1 of

Title 26, Internal Revenue Code of 1939, derived by an individual from any trade or business carried on by such individual, less the deductions allowed under such chapter which are attributable to such trade or business, plus his distributive share (whether or not distributed) of the ordinary net income or loss, as computed under section 183 of Title 26, Internal Revenue Code of 1939, from any trade or business carried on by a partnership of which he is a member:

* * * * *

Trade or business

(c) The term "trade or business", when used with reference to self-employment income or net earnings from self-employment, shall have the same meaning as when used in section 23 of Title 26, Internal Revenue Code of 1939, except that such term shall not include—

(1) The performance of the functions of a public office, other than the functions of a public office of a State or a political subdivision thereof with respect to fees received in any period in which the functions are performed in a position compensated solely on a fee basis and in which such functions are not covered under an agreement entered into by such State and the Secretary pursuant to section 418 of this title.

(2) The performance of service by an individual as an employee, other than—

(A) service described in section 410(a)(14)(B) of this title performed by an individual who has attained the age of eighteen,

(B) service described in section 410(a)(16) of this title,

(C) service described in section 410(a)(11), (12), or (15) of this title performed in the United States by a citizen of the United States,

(D) service described in paragraph (4) of this subsection, and

(E) service performed by an individual as an employee of a State or a political subdivision thereof in a position compensated solely on a fee basis with respect to fees received in any period in which such service is not covered under an agreement entered into by such State and the Secretary pursuant to section 418 of this title;

(3) The performance of service by an individual as an employee or employee representative as defined in section 1532 of Title 26, Internal Revenue Code of 1939;

(4) The performance of service by a duly ordained, commissioned, or licensed minister of a church in the exercise of his ministry or by a member of a religious order in the exercise of duties required by such order;

(5) The performance of service by an individual in the exercise of his profession as a Christian Science practitioner; or

(6) The performance of service by an individual during the period for which an exemption under section 1402(h) of Title 26, Internal Revenue Code of 1954, is effective with respect to him.

The provisions of paragraph (4) or (5) shall not apply to service (other than service performed by a member of a religious order who has taken a vow of poverty as a member of such order) performed by an individual unless an exemption under section 1402(e) of Title 26, Internal Revenue Code of 1954, is effective with respect to him.

* * * * *

§ 1402. Definitions

(a) Net earnings from self-employment.—The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in section 702(a)(9) from any trade or business carried on by a partnership of which he is a member; except that in computing such gross income and deductions and such distributive share of partnership ordinary income or loss—

(1) there shall be excluded rentals from real estate and from personal property leased with the real estate (including such rentals paid in crop shares) together with the deductions attributable thereto, unless such rentals are received in the course of a trade or business as a real estate dealer; except that the preceding provisions of this paragraph shall not apply to any income derived by the owner or tenant of land if (A) such income is derived under an arrangement, between the owner or tenant and another individual, which provides that such other individual shall pro-

duce agricultural or horticultural commodities (including livestock, bees, poultry, and fur-bearing animals and wildlife) on such land, and that there shall be material participation by the owner or tenant (as determined without regard to any activities of an agent of such owner or tenant) in the production or the management of the production of such agricultural or horticultural commodities, and (B) there is material participation by the owner or tenant (as determined without regard to any activities of an agent of such owner or tenant) with respect to any such agricultural or horticultural commodity;

(3) there shall be excluded any gain or loss—

(A) which is considered as gain or loss from the sale or exchange of a capital asset,

(B) from the cutting of timber, or the disposal of timber, coal, or iron ore, if section 631 applies to such gain or loss, or

(C) from the sale, exchange, involuntary conversion, or other disposition of property if such property is neither—

(i) stock in trade or other property of a kind which would properly be includible in inventory if on hand at the close of the taxable year, or

(ii) property held primarily for sale to customers in the ordinary course of the trade or business;

* * * * *

(2) there shall be excluded dividends on any share of

stock, and interest on any bond, debenture, note, or certificate, or other evidence of indebtedness, issued with interest coupons or in registered from by any corporation (including one issued by a government or political subdivision thereof), unless such dividends and interest (other than interest described in section 35) are received in the course of a trade or business as a dealer in stocks or securities;

* * * * *

(c) Trade or business.—The term "trade or business", when used with reference to self-employment income or net earnings from self-employment, shall have the same meaning as when used in section 162 (relating to trade or business expenses), except that such term does not include—

(1) the performance of the functions of a public office, other than the functions of a public office of a State or a political subdivision thereof with respect to fees received in any period in which the functions are performed in a position compensated solely on a fee basis and in which such functions are not covered under an agreement entered into by such State and the Secretary of Health, Education, and Welfare pursuant to section 218 of the Secial Security Act;

(2) the performance of service by an individual as an employee, other than—

(A) service described in section 3121(b)(14)

(B) performed by an individual who has attained the age of 18,

(B) service described in section 3121(b)(16),

(C) service described in section 3121(b)(11), (12), or (15) performed in the United States, (as

defined in section 3121(e) (2)) by a citizen of the United States,

(D) service described in paragraph (4) of this subsection, and

(E) service performed by an individual as an employee of a State or a political subdivision thereof in a position compensated solely on a fee basis with respect to fees received in any period in which such service is not covered under an agreement entered into by such State and the Secretary of Health, Education, and Welfare pursuant to section 218 of the Social Security Act;

* * * * *

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IN THE

Supreme Court of the United States

No. 74-1495

FLORENCE G. SHEFNER,
Petitioner,

vs.

CASPAR WEINBERGER, Secretary of Health, Education and Welfare,
Respondent.

SUPPLEMENTAL ADDENDUM

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SUPPLEMENTAL ADDENDUM

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF MISSOURI EASTERN DIVISION

MRS. IRMA W. FULBRIGHT,

Plaintiff,

vs.

SECRETARY OF HEALTH, EDUCATION AND WELFARE, CASPAR H. WEINBERGER, United States of America,

Defendant.

MEMORANDUM AND ORDER

This matter is before the Court upon the parties' cross-motions for summary judgment. Since only issues of law concerning a review of the final decision of the Secretary of Health, Education and Welfare is involved, this action is in a proper posture for judgment. *Clevenger* v. *Weinberger*, 375 F.Supp. 821 (W.D., Mo., 1974).

This is an action under Title II of the Social Security Act, as amended, codified at 42 U.S.C. §401 set seq. This review is pursuant to §405(g).

On March 11, 1971, plaintiff filed her application for retirement (old-age) insurance benefits as provided in §402 (a) of the Act. Based on her earnings record at that time, plaintiff received the sum of $4,624 in benefit payments for the months of January, 1971, through February, 1973. In a "Notice of Determination of F.I.C.A. Wages" dated

February 20, 1973, plaintiff was informed that wages reported to her record as an employee of a corporation were exempt from coverage, since such services were performed for her spouse, who, it had been determined, was self-employed. Plaintiff's claim was reconsidered and she was informed that her wages for 1968, 1969 and 1970, were not "wages" within the meaning of the Social Security Act. The time limitation for correcting the 1968 wages had expired, but all wages reported to her record for 1969 and 1970 were removed. This left plaintiff with insufficient quarters of coverage to qualify for entitlement. She was terminated effective March of 1970. She was also informed that she must refund her overpayment of $4,624.00.

On March 7th and 8th, 1974, at plaintiff's request, a hearing was held in which she appeared and testified. Plaintiff was represented by counsel and her husband also appeared and testified on her behalf.

On March 12, 1974, Administrative Law Judge rendered a decision unfavorable to plaintiff. He concluded that the plaintiff did not meet the insured status requirements for retirement (old-age) insurance benefits and that she had been overpaid $4,624.00. He further determined that plaintiff was not without fault in receiving such overpayment and is therefore liable for the amount of the overpayment. He based his conclusion on the finding that plaintiff's husband did not operate his real estate business as a corporation but, rather, was self-employed.

The Appeals Council of the Social Security Administration affirmed the decision of the Administrative Law Judge. Thus, the decision of the Administrative Law Judge stands as the final decision of the Secretary.

The two issues presented to this Court for review are:

Was the Social Security Administration correct in their determination that plaintiff's employment by the Wilbur L. Fullbright Realty Company was service in the employ of her spouse? And was the Social Security Administration correct in their determination that plaintiff was at fault in receiving old age insurance payments?

The scope of review in an action such as the one presently at bar is that the reviewing court is required to uphold the Secretary's decision even if it disagrees with it, so long as that decision is supported by substantial evidence. *Blalock* v. *Richardson*, 483 F.2d 773 (4th Cir., 1972).

Defendant Secretary has filed with the Court a transcript of the administrative hearings before the Social Security Administration which provides the factual basis for this review.

The facts indicate that plaintiff worked for the Wilbur L. Fullbright Realty Company from 1959 to 1970, but was not paid for her services prior to 1968 because of lack of company funds. Plaintiff is also a director of the company and holds the office of secretary. During the years, 1968 through 1970, plaintiff worked every day performing secretarial duties such as typing and record-keeping. Plaintiff stated that she received her salary of $7,800 annually in one lump sum. During the same period, the company had one licensed salesman named Fred Stephenson. Plaintiff's husband also sold property for the company.

The Wilbur L. Fullbright Realty Company was issued a real estate corporation license from the State of Missouri for the years, 1968 through 1970. Plaintiff's husband was licensed by Missouri as a real estate officer from 1968 through 1970. For the same years, the company also paid corporation franchise taxes and filed anti-trust affidavits

with the Missouri Secretary of State. All property listing agreements were signed by plaintiff's husband, as president of the company.

Prior to 1959, the company was jointly owned by Mr. Mohrman and plaintiff's husband. Mr. Mohrman withdrew from the company on June 16, 1959, and thereafter the only owners of stock in the company were plaintiff and her husband. Plaintiff stated that she was appointed to the office of secretary and director by her husband at an informal meeting in 1959. She stated that she owns 50% of the stock, but could not state how many shares she owns. She stated that no subsequent meetings were held except those described by plaintiff as informal meetings between her husband and herself. Plaintiff was not even sure whether stock certificates had actually been issued. No formal records were kept of any meetings.

Plaintiff testified that her husband's salary was assigned before she became involved in the company. Although no records were made of that decision, it was stated that the decision to pay her was made between her husband and herself. Her husband's salary was based on a commission for the business he brought in and he received no salary for being director or president of the company. Everything he was paid went through the company books.

Wilbur L. Fullbright, plaintiff's husband, stated that he was elected president of the original company on October 1, 1940, and has continued in that position since that time. He stated that the company has always maintained its status as a Missouri corporation and has filed all required forms, tax returns and reports. Mr. Fullbright stated that stock certificates had been issued and were kept in a safe at the company.

Plaintiff's husband testified that the corporation employed a Mr. Stephenson as a salesman. He was paid on a commission basis through the corporation. Mr. Fullbright stated that the corporation maintains a separate bank account. He stated that all the decisions for the company are made by the plaintiff and himself, although he admitted that he was the more influential. He testified that the decision to pay plaintiff a salary was based on the fact that the company had enough money to do so. The decision was arrived at informally, and the amount of $7,800 was arrived at because it was the maximum wage credit for social security purposes. He added that he wanted to pay plaintiff an income to establish social security eligibility.

In 1970, the gross earnings of the corporation were $4,-846.80, but plaintiff was still paid $7,800. Mr. Fullbright stated that he paid the corporation $7,800 in cash in 1970 from his and plaintiff's personal bank account in order to pay plaintiff. He stated that he owed the corporation certain amounts for past advances. He stated there was no meeting held on this subject. Mr. Fullbright testified that the money paid to plaintiff in 1970 was taken out of their joint account and put into the corporate account; then it was paid back to plaintiff where it was again placed in their personal joint account. Mr. Fullbright also stated that he received a substantial salary in 1968 for his services as an officer and salesman, but received nothing in other years. Mr. Fullbright testified that he filed his federal tax returns for the years, 1960 through 1967, as a self-employed individual. During this period, he stated that all monies were still channeled through the corporation, but that he filed as a self-employed individual so that his social security taxes would be lower. Plaintiff's husband also testified

that he personally is not licensed as a broker but only as an officer of the corporation. The company, as a corporation, holds a broker's license.

Plaintiff has cited cases standing for the proposition that the formation of corporate entities for the purpose of establishing eligibility for social security benefits is not improper, and that employment of one's spouse or family member by the corporation will not disqualify the spouse or family member from receiving benefits. *Stark* v. *Flemming*, 283 F.2d 410 (9th Cir., 1960); *Brannon* v. *Ribicoff*, 200 F. Supp. 697 (D.C. Mont., 1961); and *De martinez* v. *Gardner*, 291 F.Supp. 132 (D.C. Pr., 1968). This Court agrees with the holding of the aforecited cases that a corporate entity is not to be treated as a sham merely because the Secretary of Health, Education and Welfare seeks to do so. However, in the above cases, while the corporate entities were informally run and operated, salaries were paid on a regular basis to the parties in question, and no one declared himself a self-employed person under the income tax laws as in the present case.

The fact that plaintiff's salary was transferred from a personal account to the corporate account and back to the personal account, along with plaintiff's husband's filing of his federal income tax as a self-employed person, clearly indicates that the Wilbur L. Fullbright Realty Company was merely a shell. The decision of the Secretary to disregard such "flow-through" transactions is not an abuse of his discretion. The Secretary's determination that plaintiff's wages for the years, 1968, 1969 and 1970, were not "wages" is supported by the record. With regards to the Secretary's determination that an overpayment had been made to plaintiff, and that repayments should be made to

the Secretary, that determination will be reversed. It is this Court's opinion that such a recovery would be against equity and good conscience in the present case, 42 U.S.C. §404(b). In consequence,

IT IS HEREBY ORDERED that defendant shall have summary judgment against the plaintiff concerning any future retirement (old-age) insurance benefits under the Social Security Act; and

IT IS FURTHER ORDERED that plaintiff shall have summary judgment against the defendant for any recovery of overpayments to plaintiff; and

IT IS FURTHER ORDERED that costs shall be shared equally between the parties.

Dated this 26th day of March, 1975.

/s/ H. KENNETH WANGELIN
United States District Judge

In the Supreme Court of the United States

OCTOBER TERM, 1975

NO. 74-1495

FLORENCE G. SHEFNER, PETITIONER

v.

CASPAR W. WEINBERGER, SECRETARY OF HEALTH, EDUCATION, AND WELFARE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner brought this action under Section 205(g) of the Social Security Act, 49 Stat. 624, as amended, 42 U.S.C. 405(g), to review a final decision of the Secretary upholding a deduction in wife's and retirement insurance benefits in the amount of $178.30. Petitioner has worked since 1956 as a secretary for her husband, who is a self-employed attorney and certified public accountant. Petitioner applied for wife's and retirement insurance benefits in 1972. In a revised determination, the Secretary ruled that petitioner was eligible for such benefits but that benefits could not be paid to her because she had excess earnings from her employment with her husband for the taxable years 1968 through 1971. Because of these excess earnings,

a refund was demanded of $178.30 in benefits that had been paid to petitioner by mistake in May 1969 and September 1970.[1]

Before the hearing examiner, petitioner urged that because services performed in the employ of a spouse are excluded from the definition of "employment" in Section 210(a)(3)(A) of the Act, and therefore are not subject to Federal Insurance Contributions Act taxes, remuneration for such services should not constitute excess earnings for purposes of deductions from benefits (Pet. Add. 5). In rejecting this argument, the hearing examiner noted that "the Congressional definition of excess earnings for purposes of benefit deductions expressly includes, under section 203(f)(5)(C), remuneration for services which do not constitute 'employment' as defined in section 210 if such services are performed within the United States as a employee and such remuneration is not includable in computing self-employment net earnings or loss" (Pet. Add. 6). The hearing examiner specifically found that petitioner's earnings "were remuneration for services performed within the United States as an employee and were not net earnings from self-employment" (Pet. Add. 8). The hearing examiner's decision became the final decision of the Secretary when the Appeals Council denied further review (Pet. Add. 10). Petitioner then filed this action in the United States

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[1]The Secretary's authority to make deductions against Social Security benefits is provided in Section 203(b) of the Act. Deductions are allowed "on the basis of such individual's wages and self-employment * * * if * * * he is charged with excess earnings * * *." "Excess earnings" is defined in Section 203(f)(3) as "earnings * * * in excess of the product of $175 * * * multiplied by the number of months in such year."

District Court for the District of Minnesota. The district court granted summary judgment for the Secretary (Pet. Add. 11-13), and the court of appeals affirmed *per curiam* (Pet. App. 1-2).

The decision below is correct, and there is no occasion for further review. Petitioner's contentions were fully answered by the district court, on whose opinion we rely.

As the district court pointed out, the issue raised by petitioner is resolved by the unambiguous language of Section 203(f)(5)(C) of the Social Security Act,[2] which provides that for the purposes of the subsection dealing with reductions of benefits, an individual's wages shall be deemed to be on account of employment even if those wages were paid for services that do not constitute employment for Federal Insurance Contributions Act tax purposes under Section 210(a)(3)(A) of the Act. See *Gardner* v. *Travis*, 387 F.2d 508 (C.A. 10).[3] Thus a person

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[2]For this reason, the tax cases cited by petitioner (Pet. 3-5) are inapposite.

[3]In *Travis*, the court held (387 F. 2d at 513):

> Section 203(f)(5)(C) expressly makes the dictates of Section 210 inapplicable to the determination of benefits deductions. That section provides that in computing an individual's wages for the purpose of making benefit deductions, 'services which do not constitute employment as defined in section [210] of this title, performed *within the United States* by the individual as an employee * * *, shall be deemed to be employment as so defined if the remuneration for such services is not includible in computing his net earnings or net loss from self-employment.' (Emphasis added). In our words, even if a service does not fall within the Section 210(a)

is ineligible to receive social security retirement benefits if that person is still working for wages and earning the statutory maximum in earnings even if those earnings are not from covered employment. The obvious purpose of Section 203(f)(5)(C) is to exclude from benefits those persons "who have [not] ceased to labor". *Social Security Board* v. *Nierotko*, 327 U.S. 358, 364.

The petition for a writ of certiorari should therefore be denied.

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

JULY 1975.

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definition of 'employment', Section 203(f)(5)(C) requires that wages received from the performance of that service be considered in determining whether benefit deductions are warranted.